

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 8-K

CURRENT REPORT PURSUANT
TO SECTION 13 OR 15(D) OF THE
SECURITIES EXCHANGE ACT OF 1934

February 20, 2009

(Date of earliest event reported)

TELKONET, INC.
(Exact Name of Registrant as Specified in Its Charter)

Utah

(State or Other Jurisdiction of Incorporation)

000-31972
(Commission File No.)

87-0627421
(I.R.S. Employer Identification No.)

20374 Seneca Meadows Parkway, Germantown, Maryland 20876
(Address of Principal Executive Offices)

(240)-912-1800
(Registrant's Telephone Number)

Not Applicable
(Former Name or Former Address, if Changed Since Last Report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions (see General Instruction A.2. below):

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425).
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12).
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b)).
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c)).
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Item 1.01 Entry into a Material Definitive Agreement

On February 26, 2009, Telkonet, Inc. (the "Company") executed and completed a Stock Purchase Agreement (the "Agreement") with William Davis pursuant to which the Company sold, and Mr. Davis purchased, two million, eight hundred thousand shares of MSTI Holdings, Inc. common stock (the "MSTI Shares") for consideration in the aggregate principal amount of Ten Thousand Dollars (\$10,000.00).

In a related transaction, the Company entered into a Partial Release of Lien with YA Global Investments, L.P. ("YA Global"), pursuant to which, in consideration of YA Global's agreement to release its lien and security interest on the MSTI Shares, the Company paid a commitment fee to YA Global in MSTI Holdings, Inc. common stock equal to one percent (1%) of MSTI Holdings, Inc. common stock owned by the Company following the sale of the MSTI Shares (One Hundred and Fifty Seven Thousand Shares). Prior to the transaction, the Company held Eighteen Million, Five Hundred Thousand (18,500,000) Shares of MSTI Holdings, Inc. common stock.

With the reduction in holdings, the Company now holds Fifteen Million, Five Hundred and Forty Three Thousand Shares of MSTI Holdings, Inc. common stock reducing its percentage holdings in MSTI Holdings, Inc. common stock to forty nine percent (49%).

As previously reported in a Form 8-K filed on June 5, 2008, on May 30, 2008, the Company entered into a Securities Purchase Agreement with YA Global pursuant to which the Company agreed to issue and sell to the Buyer up to \$3,500,000 of secured convertible debentures (the "Debentures") and warrants to purchase (the "Warrants") up to 2,500,000 shares of the Company's Common Stock, par value \$0.001 per share (the "Common Stock"). On February 20, 2009, the Company and YA Global entered into an Agreement of Clarification pursuant to which the parties agreed upon the following clarifications to the Securities Purchase Agreement and the Debentures:

- The parties agree that the term Equity Conditions shall be clarified such that if the Company's Common Stock has not been suspended from trading and the Company has not been notified in writing that a delisting or suspension from trading is threatened or pending, the Company shall be deemed to have satisfied the conditions in clause (B) requiring that the Company be in compliance with the then effective minimum listing maintenance requirements of the exchange on which the Common Stock is listed.
 - Section 1(b) of the Debenture requires, among other things, that interest shall be paid quarterly, in arrears. The Debentures do not indicate when such quarterly interest payments begin. The parties agreed to clarify that the quarterly interest payments shall be paid on the first Business Day of each calendar quarter beginning on April 1, 2009. The parties further agreed to clarify that quarterly interest accrued to date shall be added to the principal amount outstanding under the Debentures and that each Debenture be amended to reflect the applicable increase in principal amount. The parties further agreed that the Company is not in breach of Section 2(a) of the Debentures for not making any interest payments during calendar year 2008 or the first quarter of calendar year 2009.
 - The conversion provisions contained in Section 4 of the Debentures and the exercise provisions contained in Section 2 of the Warrants do not cap such conversion or exercise provisions, as applicable, to the 19.99% Limitation. The Principal Market requires such a cap absent stockholder approval. To date the Company has not sought, nor has YA Global requested, stockholder approval for issuances of common stock in excess of the 19.99% Limitation. Accordingly, the parties agree that the 19.99% Limitation is applicable for conversion of the Debentures and exercises of the Warrants, in the aggregate and that the Company shall not be obligated to issue such shares of common stock in excess of the 19.99% Limitation unless and until the Company obtains stockholder approval in accordance with applicable Principal Market rules and regulations. Further, the Company agreed to seek stockholder approval to remove the 19.99% Limitation at its next annual meeting, to be held on or before May 31, 2009.
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Item 2.01 Completion of Acquisition or Disposition of Assets

To the extent required by Item 2.01 of Form 8-K, the information contained in or incorporated by reference into Item 1.01 of this Current Report is hereby incorporated by reference into this Item 2.01.

Item 9.01 Financial Statements and Exhibits.

(d) Exhibits

- 4.1 Stock Purchase Agreement
- 4.2 Partial Release of Lien
- 4.3 Agreement of Clarification

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

TELKONET, INC.

Date: February 26, 2009

By: /s/ Richard J. Leimbach

Richard J. Leimbach
Chief Financial Officer

STOCK PURCHASE AGREEMENT

THIS STOCK PURCHASE AGREEMENT, together with all Schedules and Exhibits to be delivered pursuant hereto (collectively, this "Agreement"), is made and shall be effective as of February 26, 2009, by and between William H. Davis, with an address of 29 Glen Green, Winchester, MA ("Buyer"), and Telkonet, Inc., a Utah corporation with an address of 20374 Seneca Meadows Parkway, Germantown, Maryland 20876 ("Seller").

BACKGROUND

Seller owns 18,500,000 shares of the common stock of MSHI Holdings, Inc. (the "Company"). Seller is interested in selling to Buyer, and Buyer is interested in purchasing from Seller, 2,800,000 shares of the common stock of the Company owned by Seller (the "Shares").

TERMS

NOW, THEREFORE, in consideration of the mutual covenants and agreements set forth in this Agreement, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto, intending to be legally bound, hereby agree as follows:

ARTICLE I

SALE OF SHARES AND CLOSING

1.01 Purchase and Sale. Seller agrees to sell to Buyer, and Buyer agrees to purchase from Seller, all of the right, title and interest of Seller in and to the Shares at the Closing (as defined in Section 1.03), free and clear of any and all liens, claims and encumbrances of any nature whatsoever, on the terms and subject to the conditions set forth in this Agreement.

1.02 Purchase Price. The aggregate purchase price ("Purchase Price") for the Shares shall be Ten Thousand Dollars (\$10,000.00), payable by Buyer to Seller.

1.03 Closing.

(a) The closing of the transactions contemplated by this Agreement (the "Closing") shall take place by the electronic exchange of documents on Friday, February 13, 2009, or at such place or on such other date as is mutually agreed upon by the parties (the "Closing Date"). The Closing shall be effective as of the close of business on the Closing Date.

(b) Subject to the conditions set forth in this Agreement, on the Closing Date or, with respect to subparagraph (i) below, as soon as reasonably practicable thereafter:

(i) Seller shall transfer to Buyer the Shares by delivering to Buyer stock certificates representing the Shares, duly endorsed for transfer or accompanied by duly executed stock powers endorsed in blank with requisite stock transfer tax stamps, if any, attached;

(ii) Buyer shall deliver the Purchase Price in accordance with Article IV hereof; and

(iii) Each of the parties hereto shall deliver to the other the documents required to be delivered pursuant to Article IV hereof, and such other certificates and documents as the parties or their respective counsel may reasonably request in order to consummate the transactions contemplated hereby.

ARTICLE II

REPRESENTATIONS AND WARRANTIES OF SELLER

As a material inducement to Buyer to enter into this Agreement and to close hereunder, Seller hereby represents and warrants to Buyer as follows:

2.01 Ownership of Capital Stock. Except as set forth in Schedule 2.01 hereto, Seller owns, beneficially and of record, all right, title and interest in and to the Shares, free and clear of any adverse interests, security interests, claims, liens, pledges, options, encumbrances, charges, agreements, voting trusts, proxies or other arrangements, restrictions or limitations of any kind. On the Closing Date, the delivery by Seller of stock certificates in the manner set forth in Section 1.03(b) hereof will transfer title to the Shares to Buyer, free and clear of any adverse claim, security interests, claims, liens, pledges, options, encumbrances, charges, agreements, voting trusts, proxies or other arrangements, restrictions or other legal or equitable limitations of any kind.

2.02 Capacity, Execution, Delivery; Valid and Binding Agreements. Seller has the sole authority and legal capacity to execute and deliver this Agreement and the other agreements contemplated hereby and to perform its respective obligations hereunder and thereunder (including, without limitation, the power to sell, transfer and convey the Shares as provided by this Agreement). This Agreement has been duly executed and delivered by Seller and constitutes the valid and binding obligation of Seller, enforceable in accordance with its terms. Except as set forth in Schedule 2.02 hereto, no consent is required with respect to Seller or the Company in connection with the execution, delivery, and performance of this Agreement or any other agreement contemplated hereby.

2.03 Incorporation and Corporate Power. The Seller is a corporation duly organized, validly existing and in good standing under the laws of the State of Utah. The Seller has full power and authority and all authorizations, licenses, permits and certifications necessary to own and operate its properties and to carry on its business as now conducted and presently proposed to be conducted.

2.04 No Breach. Except as set forth in Schedule 2.04 hereto, the execution, delivery and performance of this Agreement by Seller and the consummation by Seller of the transactions contemplated hereby do not conflict with or result in any breach of any of the provisions of, constitute a default under, result in a violation of, result in the creation of a right of termination or acceleration or any lien, security interest, charge or encumbrance upon any of the Shares or any assets of Seller or the Company, or require any authorization, consent, approval, exemption or other action by or notice to any third party, court or other governmental body, under the provisions of the Articles of Incorporation or Bylaws of Seller or the Company or any indenture, mortgage, lease, loan agreement or other agreement or instrument by which Seller or the Company is bound or affected, or any law, statute, rule or regulation or order, judgment or decree to which Seller or the Company is subject.

2.05 Governmental Authorities; Consents. Except as set forth in Schedule 2.05 hereto, Seller is not required to submit any notice, report or other filing with any governmental authority in connection with the execution or delivery by it of this Agreement or the consummation of the transactions contemplated hereby. No consent, approval or authorization of any governmental or regulatory authority or any other party or person is required to be obtained by Seller, in connection with the execution, delivery and performance of this Agreement or the transactions contemplated hereby.

2.06 Brokerage. No third party shall be entitled to receive any brokerage commissions, finder's fees, fees for financial advisory services or similar compensation in connection with the transactions contemplated by this Agreement based on any arrangement or agreement made by or on behalf of Seller.

2.07 Disclosure. No representation or warranty by Seller hereunder, nor any statement contained in any certificate, schedule, list or other writing furnished or to be furnished by Seller to Buyer pursuant to this Agreement (i) contains or shall contain any untrue statement of a material fact, or (ii) omits or shall omit to state a material fact necessary in order to make the statements contained herein or therein not misleading.

ARTICLE III

REPRESENTATIONS AND WARRANTIES OF BUYER

As a material inducement to Seller to enter into this Agreement and to close hereunder, Buyer hereby represents and warrants to Seller as follows:

3.01 Execution, Delivery; Valid and Binding Agreement. This Agreement has been duly executed and delivered by Buyer and constitutes the valid and binding obligation of Buyer, enforceable in accordance with its terms.

3.02 Investigation; Economic Risk. Buyer acknowledges that it has knowledge and experience in financial and business matters such that it is capable of evaluating the risks of the transactions contemplated by this Agreement. The parties acknowledge and agree that nothing in this Section 3.02 shall limit or modify any representation or warranty of the Seller in Section 2 hereof, or the right of Buyer to rely thereon.

3.03 Buyer acknowledges that the Shares will initially be "restricted securities" (as such term is defined in Rule 144 promulgated under the Securities Act of 1933, as amended ("Rule 144")), and that the Shares will bear substantially the following restrictive legend:

The shares represented by this certificate have not been registered under the Securities Act of 1933 (the "Act"), and are Restricted Securities as that term is defined in Rule 144 under the Act, and requires written release from either the issuing company or their attorney prior to legend removal.

ARTICLE IV

CLOSING

4.01 Seller's Documents. At the Closing, or as soon as reasonably practicable thereafter, Seller shall deliver to Buyer the stock certificates issued to Seller representing the Shares, duly endorsed for transfer or accompanied by a duly executed stock power, with requisite stock transfer stamps, if any, attached.

4.02 Buyer's Documents. At the Closing, Buyer shall deliver to Seller the Purchase Price in immediately available funds by wire transfer to an account designated by Seller.

4.03 Conditions to Closing. Each of Buyer and Seller shall have performed and complied in all material respects with all agreements, obligations and conditions contained in this Agreement that are required to be performed or complied with by it or them on or before the Closing.

ARTICLE V

SURVIVAL; INDEMNIFICATION

5.01 Survival of Representations and Warranties. Notwithstanding any investigation made by or on behalf of any of the parties hereto or the results of any such investigation and notwithstanding the participation of such party in the Closing, the representations and warranties contained in Article II and Article III hereof shall survive the Closing.

5.02 Indemnification. (a) Seller shall indemnify in full Buyer, his attorneys, agents, successors and assigns (collectively, the "Buyer Indemnified Parties") and hold them harmless against any loss, liability, deficiency, damage, expense or cost (including reasonable legal expenses, including costs) (collectively, "Losses"), which Buyer Indemnified Parties may suffer, sustain or become subject to, as a result of (i) any breach of any of the representations or warranties of Seller contained in this Agreement or in any exhibit, schedule or certificate delivered or to be delivered by or on behalf of Seller pursuant to the terms of this Agreement, (ii) any breach of, or failure to perform, any agreement of Seller contained in this Agreement. (b) Buyer shall indemnify and hold harmless Seller, including its managers, members, officers, directors, employees, attorneys, agents, successors and assigns (collectively, the "Seller Indemnified Parties") against all Losses that Seller Indemnified Parties may suffer, sustain, or become subject to as a result of (i) any breach of any of the representations or warranties of Buyer contained in this Agreement or in any exhibit, schedule or certificate delivered or to be delivered by or on behalf of Buyer pursuant to the terms of this Agreement, (ii) any breach of, or failure to perform, any agreement of Buyer contained in this Agreement.

5.03 Method of Asserting Claims. As used herein, an "Indemnified Party" shall refer to the party entitled to indemnification hereunder, the "Indemnified Party" and the "Indemnifying Party" shall refer to the party obligated to provide the indemnity.

(a) In the event that any of the Indemnified Parties is made a defendant in or party to any action or proceeding, judicial or administrative, instituted by any third party for the liability or the costs or expenses of which are Losses (any such third party action or proceeding being referred to as a "Claim"), the Indemnified Party shall give the Indemnifying Party prompt notice thereof. The failure to give such notice shall not affect any Indemnified Party's ability to seek reimbursement unless such failure has materially and adversely affected the Indemnifying Party's ability to defend successfully a Claim. The Indemnifying Party shall be entitled to contest and defend such Claim. Notice of the intention to contest and defend shall be given by the Indemnifying Party to the Indemnified Party within 20 business days after the Indemnified Party's notice of such Claim (but, in all events, at least five business days prior to the date that an answer to such Claim is due to be filed). Such contest and defense shall be conducted by reputable attorneys engaged by the Indemnifying Party and approved by the Indemnified Parties. The Indemnified Party shall be entitled at any time, at its own cost and expense (which expense shall not constitute a Loss), to participate in such contest and defense and to be represented by attorneys of its own choosing. If the Indemnified Party elects to participate in such defense, the Indemnified Party will cooperate with the Indemnifying Party in the conduct of such defense. Neither the Indemnified Party nor the Indemnifying Party may concede, settle or compromise any Claim without the consent of the other party, which consents will not be unreasonably withheld. Notwithstanding the foregoing, (i) if a Claim seeks equitable relief or (ii) if the subject matter of a Claim relates to the ongoing business of any of the Indemnified Parties, which Claim, if decided against any of the Indemnified Parties, would materially adversely affect the ongoing business or reputation of any of the Indemnified Parties, then, in each such case, the Indemnified Parties alone shall be entitled to contest, defend and settle such Claim in the first instance and, if the Indemnified Parties do not contest, defend or settle such Claim, the Indemnifying Party shall then have the right to contest and defend (but not settle) such Claim.

(b) In the event any Indemnified Party should have a claim against any Indemnifying Party that does not involve a Claim, the Indemnified Party shall deliver a notice of such claim with reasonable promptness to the Indemnifying Party. If the Indemnifying Party notifies the Indemnified Party that it does not dispute the claim described in such notice or fails to notify the Indemnified Party within 30 days after delivery of such notice by the Indemnified Party whether the Indemnifying Party disputes the claim described in such notice, the Loss in the amount specified in the Indemnified Party's notice will be conclusively deemed a liability of the Indemnifying Party and the Indemnifying Party shall pay the amount of such Loss to the Indemnified Party on demand. If the Indemnifying Party has timely disputed its Liability with respect to such claim, then such dispute shall be resolved pursuant to the provisions of Section 6.05 below.

ARTICLE VI

GENERAL PROVISIONS

6 . 0 1 Expenses. Except as otherwise expressly provided for herein, Seller and Buyer will pay all of their own expenses (including attorneys' and accountants fees) in connection with the negotiation of this Agreement, the performance of their respective obligations hereunder and the consummation of the transactions contemplated by this Agreement.

6.02 Further Assurances. Seller and Buyer agree that, on and after the Closing Date, each shall take all appropriate action and execute any documents, instruments or conveyances of any kind which may be reasonably requested by the other party hereto to carry out any of the provisions hereof.

6 . 0 3 Amendment and Waiver. This Agreement may not be amended or waived except in a writing executed by the party against which such amendment or waiver is sought to be enforced. No course of dealing between or among any persons having any interest in this Agreement will be deemed effective to modify or amend any part of this Agreement or any rights or obligations of any person under or by reason of this Agreement.

6.04 Notices. All notices, demands and other communications to be given or delivered under or by reason of the provisions of this Agreement shall be in writing and shall be deemed to have been given when personally delivered or sent by nationally recognized overnight courier service. Notices, demands and communications to Buyer and Seller will, unless another address is specified in writing, be sent :

If to Buyer: At the address indicated above, Attn.: William H. Davis

If to Seller: At the address indicated above, Attn: Jason Tienor

With a copy to: Howard J. Barr at the Seller's address indicated above

6.05 Arbitration. Neither party shall institute a proceeding in any court or administrative agency to resolve a dispute between the parties hereunder, whether arising prior to or after the Closing Date, before that party has sought to resolve the dispute through direct negotiation with the other party. If the dispute is not resolved within three weeks after a demand for direct negotiation, the parties shall resolve the dispute through arbitration, which shall be binding, before a single arbitrator pursuant to the Commercial Arbitration Rules of the American Arbitration Association (the "Association"). The place of arbitration shall be Philadelphia, Pennsylvania. The arbitrator shall be selected by the joint agreement of Buyer and Seller, but if they do not agree within a reasonable period of time, the selection shall be made pursuant to the rules from the panels of the arbitrators maintained by the Association. The arbitrator shall render his decision within one hundred eighty (180) days of appointment. Any award rendered by the arbitrator shall be conclusive and binding upon the parties hereto; provided, however, that any such award shall be accompanied by a written opinion of the arbitrator giving the reasons for the award. This provision for arbitration shall be specifically enforceable by the parties and the decision of the arbitrator in accordance herewith shall be final and binding and there shall be no right of appeal there from. Judgment upon the award rendered by the arbitration may be entered by a court having jurisdiction thereof. The costs and expenses of arbitration, including attorneys' fees and expenses of the arbitrator shall be paid entirely by the Seller. The arbitrator shall not be permitted to award punitive or similar type damages under any circumstances. This arbitration provision shall constitute the sole and exclusive remedy for any dispute under this Agreement.

6.06 Assignment. This Agreement and all of the provisions hereof will be binding upon and inure to the benefit of the parties hereto and their respective successors and permitted assigns, except that neither this Agreement nor any of the rights, interests or obligations hereunder may be assigned by any party hereto without the prior written consent of the other party hereto.

6.07 Severability. Whenever possible, each provision of this Agreement will be interpreted in such manner as to be effective and valid under applicable law, but if any provision of this Agreement is held to be prohibited by or invalid under applicable law, such provision will be ineffective only to the extent of such prohibition or invalidity, without invalidating the remainder of such provision or the remaining provisions of this Agreement.

6.08 Complete Agreement. This Agreement, and the Exhibits and Schedules and the other documents referred to herein, contain the complete agreement between the parties and supersede any prior understandings, agreements or representations by or between the parties, written or oral, which may have related to the subject matter hereof in any way.

6.09 Counterparts. This Agreement may be executed in one or more counterparts, any of which need not contain the signatures of more than one party, but all such counterparts taken together will constitute one and the same instrument.

6.10 Governing Law. The internal law, without regard to conflicts of laws principles, of the Commonwealth of Pennsylvania will govern all questions concerning the construction, validity and interpretation of this Agreement and the performance of the obligations imposed by this Agreement.

6.11 Headings. The headings of the several articles and sections of this Agreement are inserted for convenience of reference only and shall not constitute part of this Agreement.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the day and year first above written.

BUYER

By: /s/ William H. Davis
Name: William H. Davis
Title:

TELKONET, INC.

By: /s/ Richard J. Leimbach
Name: Richard J. Leimbach
Title: CFO

Schedule 2.01

Buyer acknowledges that YA Global Investments LP holds a security interest in the Shares and that its consent is necessary to the consummation of the transaction contemplated herein.

Schedule 2.02

Buyer acknowledges that YA Global Investments LP holds a security interest in the Shares and that its consent is necessary to the consummation of the transaction contemplated herein.

Schedule 2.04

Buyer acknowledges that YA Global Investments LP holds a security interest in the Shares and that its consent is necessary to the consummation of the transaction contemplated herein.

Schedule 2.05

The sale of the Shares constitutes the entry into a material definitive agreement not made in the ordinary course of business of the Seller that is material to the Seller and is therefore reportable pursuant to the Securities Exchange Act of 1934 and the rules of the Securities Exchange Administration.

PARTIAL RELEASE OF LIEN

THIS PARTIAL RELEASE OF LIEN, dated of as February 20, 2009, is by and between **TELKONET, INC.**, a Utah corporation (the "Company"), the guarantors listed on the signature page hereto (the "Guarantors") and **YA GLOBAL INVESTMENTS, L.P.** ("YA Global"). All capitalized terms used herein shall have the respective meanings assigned thereto in the Transaction Documents (as defined below) unless otherwise defined herein.

WITNESSETH:

WHEREAS, in connection with that certain Securities Purchase Agreement dated as of May 30, 2008 between the Company and YA Global (the "SPA") and the Secured Convertible Debentures (the "Debentures") issued to YA Global thereunder, the Company, the Guarantors and YA Global entered into a Security Agreement dated as of May 30, 2008. The SPA, the Debentures, the Security Agreement, and all documents entered into in connection therewith are referred to herein collectively as the "Transaction Documents".

WHEREAS, pursuant to the Security Agreement, the Company pledged and assigned certain collateral to YA Global to secure its payment obligations under the Transaction Documents (the "Obligations"), which collateral includes, without limitation, 18,500,000 shares (the "Pledged Shares") of common stock of MTSI Holdings, Inc. ("MSTI").

WHEREAS, the Company desires to sell 2,800,000 Pledged Shares which are subject to the Security Agreement and use the proceeds to repay a portion of the Obligations.

WHEREAS, on the terms and conditions set forth herein, YA Global desires to consent to the sale by the Company of 2,800,000 Pledged Shares and release its lien and security interest thereon.

NOW, THEREFORE, in consideration of the foregoing, and the respective agreements, warranties and covenants contained herein, the parties hereto agree, covenant and warrant as follows:

1. Conditions.

YA Global hereby consents to the sale by the Company of 2,800,000 Pledged Shares, subject to the following conditions:

(a) The minimum proceeds received from the sale shall be \$10,000.

(b) The Company shall use the proceeds from the sale to pay the interest when due on the Debentures.

(c) The proceeds shall be applied first to the quarterly payment of accrued and unpaid interest on April 1, 2009 and second to subsequent quarterly payments of accrued and unpaid interest on the Debentures. Pending payment the proceeds shall be held in a separate escrow account established by the Company.

(d) The sale of the 2,800,000 Pledged Shares shall occur on or before February 27, 2009.

2. Release of Lien; Waiver of Section 7.1 of the Security Agreement.

(a) In connection with (i) the sale of 2,800,000 Pledged Shares pursuant to the terms and conditions set forth in Section 1 above and (ii) the transfer of the Commitment Fee Shares (as defined below), YA Global agrees, to release its lien and security interest on such Pledged Shares and the Commitment Fee Shares. YA Global agrees to promptly file all UCC termination statements and to execute such additional documents, instruments, and agreements that are reasonably required in order to release its lien and security interest on the 2,800,000 Pledged Shares and the Commitment Fee Shares. The Company agrees to pay the reasonable actual costs and fees incurred by YA Global in connection with such release, which cost shall not exceed \$2,500 without the Company's prior written consent. The release of the 2,800,000 Pledged Shares and the Commitment Fee Shares shall not alter, vary or diminish the force and effect of the Security Agreement or any other security documents with respect to the remainder of the collateral and any and all liens and security interests created by any such documents, or otherwise, in favor of YA Global shall remain in full force and effect with respect to the remaining collateral.

(b) In connection with the (i) sale of 2,800,000 Pledged Shares pursuant to the terms and conditions set forth in Section 1 above and (ii) the transfer of the Commitment Fee (as defined below), YA Global agrees to waive compliance with Section 7.1 of the Security Agreement.

3. Commitment Fee.

(a) In consideration for YA Global's consent to the Company's sale of 2,800,000 Pledged Shares and the release of its lien and security interest on the 2,800,000 Pledged Shares, the Company agrees to pay YA Global a commitment fee payable in MSTI common stock equal to 1% of MSTI common stock owned by the Company following the sale of the 2,800,000 Pledged Shares (the "Commitment Fee Shares").

(b) In connection with the transfer of the Commitment Fee Shares, YA Global represents, warrants and covenants as follows:

(i) Investment Purpose. YA Global is acquiring the Commitment Fee Shares for its own account for investment only and not with a view towards, or for resale in connection with, the public sale or distribution thereof. YA Global does not presently have any agreement or understanding, directly or indirectly, with any Person to distribute any of the Commitment Fee Shares.

(ii) Accredited Investor Status. YA Global is an "Accredited Investor" as that term is defined in Rule 501(a)(3) of Regulation of the Securities Act of 1933, as amended (the "Securities Act"). YA Global is not a registered broker-dealer under Section 15 of the Securities Exchange Act of 1934, as amended.

(iii) Reliance on Exemptions. YA Global understands that the Commitment Fee Shares are being transferred to it in reliance on specific exemptions from the registration requirements of United States federal and state securities laws and that the Company is relying in part upon the truth and accuracy of, and YA Global's compliance with, the representations, warranties and covenants of YA Global set forth herein in order to determine the availability of such exemptions and the eligibility of YA Global to acquire the Commitment Fee Shares.

(iv) Transfer or Resale. YA Global understands that: (i) the Commitment Fee Shares have not been and are not being registered under the Securities Act or any state securities laws, and may not be offered for sale, sold, assigned or transferred unless (A) subsequently registered, (B) YA Global shall have delivered to MSTI an opinion of counsel, in a generally acceptable form, to the effect that such Commitment Fee Shares to be sold, assigned or transferred may be sold, assigned or transferred pursuant to an exemption from such registration requirements, or (C) YA Global provides MSTI with assurances reasonably acceptable to MSTI that such Commitment Fee Shares can be sold, assigned or transferred pursuant to Rule 144, Rule 144(k), or Rule 144A promulgated under the Securities Act, as amended (or a successor rule thereto) (collectively, "Rule 144"), in each case following the applicable holding period set forth therein. YA Global acknowledges that neither MSTI nor any other person is under any obligation to register the Commitment Fee Shares under the Securities Act or any state securities laws or to comply with the terms and conditions of any exemption thereunder.

(v) Legends. YA Global acknowledges that the Commitment Fee Shares shall bear a restrictive legend in substantially the following form:

THE SECURITIES REPRESENTED BY THIS CERTIFICATE HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933. AS AMENDED, OR APPLICABLE STATE SECURITIES LAWS. THE SECURITIES HAVE BEEN ACQUIRED SOLELY FOR INVESTMENT PURPOSES AND NOT WITH A VIEW TOWARD RESALE AND MAY NOT BE OFFERED FOR SALE, SOLD TRANSFERRED OR ASSIGNED IN THE ABSENCE OF AN EFFECTIVE REGISTRATION STATEMENT FOR THE SECURITIES UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR APPLICABLE STATE SECURITIES LAWS, OR AN OPINION OF COUNSEL, IN A GENERALLY ACCEPTABLE FORM, THAT REGISTRATION IS NOT REQUIRED UNDER SAID ACT OR APPLICABLE STATE SECURITIES LAWS.

(c) In connection with the transfer of the Commitment Fee Shares the Company represents, warrants, and covenants as follows:

(i) The Company owns, beneficially and of record, all right, title and interest in and to the Commitment Fee Shares, free and clear of any adverse interests, security interests, claims, liens, pledges, options, encumbrances, charges, agreements, voting trusts, proxies or other arrangements, restrictions or limitations of any kind, except for the security interest granted to YA Global. Upon release of the Commitment Fee Shares from the pledge in accordance herewith, title to the Commitment Fee Shares will transfer to YA Global, free and clear of any adverse claim, securities interests, claims, liens, pledges, options, encumbrances, charges, agreements, voting trusts, proxies or other arrangements, restrictions or other legal or equitable limitations of any kind arising from actions of, or inactions by, the Company.

4. Effect of this Agreement. Except as modified pursuant hereto, no other changes or modifications to the Transaction Documents are intended or implied and in all other respects the Transaction Documents are hereby specifically ratified, restated and confirmed by all parties hereto as of the effective date hereof.

[SIGNATURE PAGE IMMEDIATELY TO FOLLOW]

IN WITNESS WHEREOF, this Agreement is executed and delivered as of the day and year first above written.

COMPANY:
Telkonet, Inc.

By: /s/ Jason L. Tienor
Name: Jason L. Tienor
Title: President & CEO

GUARANTOR:
Ethostream LLC:

By: /s/ Jason L. Tienor
Name: Jason L. Tienor
Title: President & CEO

GUARANTOR:
Telkonet Communications Inc.:

By: /s/ Jason L. Tienor
Name: Jason L. Tienor
Title: President & CEO

SECURED PARTY:
YA Global Investments, L.P.

By: Yorkville Advisors, LLC
Its: Investment Manager

By: /s/ Troy Rillo
Name: Troy Rillo
Title: Sr. Managing Director

AGREEMENT OF CLARIFICATION

THIS AGREEMENT OF CLARIFICATION, dated of as February 20, 2009, is by and between **TELKONET, INC.**, a Utah corporation (the "Company"), and **YA GLOBAL INVESTMENTS, L.P.** ("YA Global"). All capitalized terms used herein shall have the respective meanings assigned thereto in the Debentures (as defined below) unless otherwise defined herein.

WITNESSETH:

WHEREAS, the Company issued Secured Convertible Debentures (the "Debentures") and Warrants to purchase Common Stock (the "Warrants") to YA Global pursuant to the terms of a Securities Purchase Agreement between the Company and YA Global dated as of May 30, 2008 (the "Securities Purchase Agreement");

WHEREAS, the Debentures include a definition of the term Equity Conditions;

WHEREAS, the Company and YA Global wish to clarify clause (B) of the definition of the term Equity Condition;

WHEREAS, the Debentures require that interest shall be paid quarterly but do not indicate when such quarterly payments begin;

WHEREAS, the Debentures and the Warrants, collectively, can only be converted into, or exercised for, as applicable up to 19.99% of shares of Common Stock outstanding on the date the Securities Purchase Agreement was entered into (the "Exchange Cap") pursuant to the Principal Market rules;

WHEREAS, the parties wish to clarify the Exchange Cap and provide for the Company to seek stockholder approval to remove the Exchange Cap;

WHEREAS, the Company and YA Global wish to clarify when the quarterly interest payment should begin.

NOW, THEREFORE, in consideration of the foregoing and the respective agreements, warranties and covenants contained herein, the parties hereto agree, covenant and warrant as follows:

1. Equity Conditions Definition.

(a) The term Equity Conditions as used in the Debenture requires in clause (ii)(B) that the Company be in compliance with the then effective minimum listing maintenance requirements of the exchange on which the Common Stock is listed regardless of whether the Company has been notified in writing that a delisting or suspension of trading is threatened or pending. The parties acknowledge that the NASDAQ and other Principal Markets have temporarily suspended certain of their minimum listing maintenance requirements. The parties agree that if the Company's Common Stock has not been suspended from trading and the Company has not been notified in writing that a delisting or suspension from trading is threatened or pending, the Company shall be deemed to have satisfied the conditions in clause (B).

(b) The term Equity Conditions shall be clarified as follows:

“Equity Conditions” means that each of the following conditions: (i) on each day during the period beginning two (2) weeks prior to the applicable date of determination and ending on and including the applicable date of determination (the “Equity Conditions Measuring Period”), either (x) the Underlying Shares Registration Statement filed pursuant to the Registration Rights Agreement shall be effective and available for the resale of all applicable shares of Common Stock to be issued in connection with the event requiring determination or (y) all applicable shares of Common Stock to be issued in connection with the event requiring determination shall be eligible for sale without restriction and without the need for registration under any applicable federal or state securities laws; (ii) on each day during the Equity Conditions Measuring Period, the Common Stock is designated for quotation on the Principal Market and shall not have been suspended from trading on such exchange or market nor shall delisting or suspension by such exchange or market be threatened or pending in writing by such exchange or market; (iii) during the Equity Conditions Measuring Period, the Company shall have delivered Conversion Shares upon conversion of the Debentures to the Holder on a timely basis as set forth in Section 4(b) (ii) hereof; (iv) any applicable shares of Common Stock to be issued in connection with the event requiring determination may be issued in full without violating Section 4(c) hereof and the rules or regulations of the Primary Market; (v) during the Equity Conditions Measuring Period, there shall not have occurred either (A) an Event of Default or (B) an event that with the passage of time or giving of notice would constitute an Event of Default; and (vii) the Company shall have no knowledge of any fact that would cause (x) the Registration Statements required pursuant to the Registration Rights Agreement not to be effective and available for the resale of all applicable shares of Common Stock to be issued in connection with the event requiring determination or (y) any applicable shares of Common Stock to be issued in connection with the event requiring determination not to be eligible for sale without restriction and without the need for registration under any applicable federal or state securities laws.

2. Payment of Interest.

(a) Section 1(b) of the Debenture requires, among other things, that interest shall be paid quarterly, in arrears. The Debentures do not indicate when such quarterly interest payments begin. The parties hereby agree that the quarterly interest payments shall be paid on the first Business Day of each calendar quarter beginning on April 1, 2009. The parties further agree that quarterly interest accrued to date shall be added to the principal amount outstanding under the Debentures. Each Debenture shall be amended, if necessary, to reflect the applicable increase in principal amount. The parties agree also that the Company is in not in breach of Section 2(a) of the Debentures for not making any interest payments during calendar year 2008 or the first quarter of calendar 2009.

(b) Section 1(b) of the Debentures shall be clarified as follows:

Interest. Interest shall accrue on the outstanding principal balance hereof at an annual rate equal to thirteen percent (13%) (“Interest Rate”). Interest shall be calculated on the basis of a 365-day year and the actual number of days elapsed, to the extent permitted by applicable law. Interest hereunder shall be paid quarterly, in arrears (*on the first Business Day of each calendar quarter beginning on April 1, 2009*), and on the Maturity Date (or sooner as provided herein) to the Holder or its assignee in whose name this Debenture is registered on the records of the Company regarding registration and transfers of Debentures at the option of the Company in cash.

3. Exchange Cap.

(a) The conversion provisions contained Section 4 of the Debentures and the exercise provisions contained Section 2 of the Warrants do not cap such conversion or exercise provisions, as applicable, to the Exchange Cap. The Principal Market requires such a cap absent stockholder approval. To date the Company has not sought, nor has YA Global requested, stockholder approval for issuances of Common Stock in excess of the Exchange Cap. Accordingly, the parties agree that the Exchange Cap is applicable for conversion of the Debentures and exercises of the Warrants, in the aggregate.

(b) Section (4)(e) Limitations on Conversions of the Debentures shall be clarified to add a new paragraph (iii) as follows:

(iii) Exchange Cap. Notwithstanding anything contained herein to the contrary, the number of shares of Common Stock issuable by the Company and acquirable by the holder pursuant to the terms of this Debenture, all other Debentures and the Warrants shall not exceed an aggregate of 19.99% of the total issued and outstanding shares (calculated in accordance with applicable Principal Market rules and regulations) of the Company’s Common Stock (subject to appropriate adjustment for stock splits, stock dividends, or other similar recapitalizations affecting the Common Stock) or otherwise violate the Company’s obligations under the rules and regulations of the Principal Market (the “Exchange Cap”), unless stockholder approval shall first be obtained. The Company shall not be obligated to issue such shares of Common Stock in excess of the Exchange Cap unless and until the Company obtains stockholder approval in accordance with applicable Principal Market rules and regulations.

(c) Section 2(a) of the Warrants shall be clarified to add a new penultimate paragraph as follows:

Notwithstanding anything contained herein to the contrary, the number of shares of Common Stock issuable by the Company and acquirable by the holder pursuant to the terms of this Warrant and the Debentures shall not exceed an aggregate of 19.99% of the total issued and outstanding shares (calculated in accordance with applicable Principal Market rules and regulations) of the Company's Common Stock (subject to appropriate adjustment for stock splits, stock dividends, or other similar recapitalizations affecting the Common Stock) or otherwise violate the Company's obligations under the rules and regulations of the Principal Market (the "Exchange Cap"), unless stockholder approval shall first be obtained. The Company shall not be obligated to issue such shares of Common Stock in excess of the Exchange Cap unless and until the Company obtains stockholder approval in accordance with applicable Principal Market rules and regulations.

(d) The Company agrees to seek stockholder approval to remove the Exchange Cap at its next annual meeting, which annual meeting shall be held on or before May 31, 2009.

4. Effect of this Agreement. Except as modified pursuant hereto, no other changes or clarification to the Debentures are intended or implied.

[SIGNATURE PAGE IMMEDIATELY TO FOLLOW]

COMPANY:
Telkonet, Inc.

By: /s/ Jason L. Tienor
Name: Jason L. Tienor
Title: President & CEO

YA Global Investments, L.P.

By: Yorkville Advisors, LLC
Its: Investment Manager

By: /s/ Troy Rillo
Name: Troy Rillo
Title: Senior Managing Director